

# **Report of the Auditor General to the Gauteng Provincial Legislature and the Council on the City of Johannesburg Metropolitan Municipality**

## **Report on the consolidated and separate financial statements**

### **Introduction**

1. I have audited the consolidated and separate financial statements of the City of Johannesburg Metropolitan Municipality and its subsidiaries set out on pages ... to ..., which comprise the consolidated and separate statement of financial position as at 30 June 2014, the consolidated and separate statement of financial performance, statement of changes in net assets, cash flow statement and the statement of comparison of budget and actual amounts for the year then ended, as well as the notes, comprising a summary of significant accounting policies and other explanatory information.

### **Accounting officer's responsibility for the consolidated and separate financial statements**

2. The accounting officer is responsible for the preparation and fair presentation of these consolidated and separate financial statements in accordance with South African Standard of Generally Recognised Accounting Practice (SA Standards of GRAP), Division of Revenue Act (DoRA) and the requirements of the Municipal Finance Management Act of South Africa, 2003 (Act No.56 of 2003) (MFMA) and for such internal control as the accounting officer determines is necessary to enable the preparation of consolidated and separate financial statements that are free from material misstatement, whether due to fraud or error.

### **Auditor-general's responsibility**

3. My responsibility is to express an opinion on these consolidated and separate financial statements based on my audit. I conducted my audit in accordance with the Public Audit Act of South Africa, 2004 (Act No. 25 of 2004) (PAA), the general notice issued in terms thereof and International Standards on Auditing. Those standards require that I comply with ethical requirements, and plan and perform the audit to obtain reasonable assurance about whether the consolidated and separate financial statements are free from material misstatement.
4. An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the consolidated and separate financial statements. The procedures selected depend on the auditor's judgement, including the assessment of the risks of material misstatement of the consolidated and separate financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the consolidated and separate financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of accounting estimates made by management, as well as evaluating the overall presentation of the consolidated and separate financial statements.

5. I believe that the audit evidence I have obtained is sufficient and appropriate to provide a basis for my audit opinion.

## **Opinion**

6. In my opinion, the consolidated and separate financial statements present fairly, in all material respects, the financial position of the City of Johannesburg Metropolitan Municipality as at 30 June 2014 and its financial performance and cash flows for the year then ended, in accordance with SA Standards of GRAP, DoRA and the requirements of the MFMA.

## **Emphasis of matters**

7. I draw attention to the matters below. My opinion is not modified in respect of these matters:

## **Significant uncertainties**

8. As disclosed in note 52 to the financial statements, the municipality is the defendant in various lawsuits. The ultimate outcome of these matters cannot currently be determined and reliably measured; therefore no provision for any liabilities that may result has been made in the financial statements.

## **Restatement of corresponding figures**

9. As disclosed in note 53 to the financial statements, the corresponding figures for 30 June 2013 have been restated as a result of various errors identified during the year ended 30 June 2014.

## **Material Losses**

### **Electricity Losses**

10. As disclosed in note 54 to the consolidated financial statements, material losses amounting to R2 136 430 000 (2013: R2 144 741 000) were incurred as a result of electricity distribution losses which represent 28% (2013: 26%) of total electricity available for sale.
11. The total technical losses of electricity amounted to R1 573 988 000 (2013: R1 390 439 000). Non-technical losses amounted to R742 442 000 (2013: R754 332 000) and are due to unauthorised consumption, tampering and faulty meters.

### **Water Losses**

12. As disclosed in note 54 to the consolidated financial statements, material losses amounting to R1 160 000 000 (2013: R820 600 000) were incurred as a result of water distribution losses which represent 35, 7% (2013: 28, 9%) of total water available for sale.
13. The total level of physical losses of water amounted to R308 600 000 (2012-13: R278 200 000). The total level of commercial losses amounted to R851 100 000 (2012-13: R542 300 000) and are mainly due to pipe bursts, deterioration of water infrastructure and unauthorised consumption.

## **Material Impairment**

14. As disclosed in note 10 to the financial statements, consumer debtors have been significantly impaired. The impairment of the debtors amounts to R15 480 874 000 (2013: R14 368 788 000) which represent 76% (2013: 78%) of consumer debtors and the contribution to provision for doubtful debts for the year under review amounted to R2 676 087 000 (2013: R2 595 398 000).

## **Additional matters**

15. I draw attention to the matters below. My opinion is not modified in respect of these matters:

## **Unaudited supplementary schedules**

16. The supplementary information set out on pages XX to XX does not form part of the consolidated and separate financial statements and is presented as additional information. I have not audited these schedules and accordingly I do not express an opinion thereon.

## **Unaudited disclosure notes**

17. In terms of section 125(2) (e) of the MFMA the municipality is required to disclose particulars of non-compliance with the MFMA. This disclosure requirement did not form part of the audit of the consolidated and separate financial statements and accordingly I do not express an opinion thereon.

## **Report on other legal and regulatory requirements**

18. In accordance with the PAA and the general notice issued in terms thereof, I report the following findings relevant to the reported performance against predetermined objectives for selected development priorities presented in the annual performance report, compliance with legislation as well as internal control. The objective of my tests was to identify reportable findings as described under each subheading but not to gather evidence to express assurance on these matters. Accordingly, I do not express an opinion or conclusion on these matters.

### **Predetermined objectives**

19. I performed procedures to obtain evidence about the usefulness and reliability of the reported performance information for the following selected development priorities presented in the annual performance report of the municipality for the year ended 30 June 2014:
- Development priority 1: Sustainable service cluster pp. 193 – 202
  - Development priority 2: Economic growth cluster pp. 173 - 175
  - Development priority 3: Governance cluster pp. 184 - 189
20. I evaluated the reported performance information against the overall criteria of usefulness and reliability.

21. I evaluated the usefulness of the reported performance information to determine whether it is presented in accordance with the National Treasury's annual reporting principles and whether the reported performance was consistent with the planned development priorities. I further performed tests to determine whether indicators and targets were well defined, verifiable, specific, measurable, time bound and relevant, as required by the National Treasury's *Framework for managing programme performance information (FMPPPI)*.
22. I assessed the reliability of the reported performance information to determine whether it was valid, accurate and complete.
23. The material findings in respect of the selected development priorities are as follows:

## **Development priority 1: Sustainable service cluster**

### **Usefulness of reported performance information**

#### **Reported targets not consistent with planned targets**

24. Section 41(c) of the Municipal Systems Act (MSA) requires the integrated development plan to form the basis for the annual report, therefore requiring consistency of objectives, indicators and targets between planning and reporting documents. A total of 32% of the reported indicators and targets were not consistent with those in the approved integrated development plan. This was due to lack of adequate review by management of reported performance information against predetermined objectives detailed in the Service Delivery Budgets Implementation Plan (SDBIP).

#### **Performance targets not specific**

25. The FMPPPI requires that institutions should have appropriate systems to collect, collate, verify and store performance information to ensure valid, accurate and complete reporting of actual achievements against planned objectives, indicators and targets. The information presented with respect to sustainable services objective was not reliable when compared to the source information and/or evidence provided. This was due to the lack of standard operating procedures for the accurate recording of actual achievements, monitoring of the completeness of source documentation in support of actual achievements, frequent review of validity of reported achievements against source documentation.

### **Reliability of reported performance information**

26. The FMPPPI requires that institutions should have appropriate systems to collect, collate, verify and store performance information to ensure valid, accurate and complete reporting of actual achievements against planned objectives, indicators and targets. The information presented with respect to sustainable services objective was not reliable when compared to the source information and/or evidence provided. This was due to the lack of standard operating procedures for the accurate recording of actual achievements, monitoring of the completeness of source documentation in support of actual achievements, frequent review of validity of reported achievements against source documentation.

## **Development priority 2: Economic growth cluster**

### **Usefulness of reported performance information**

#### **Reported targets not consistent with planned targets**

27. Section 41(c) of the MSA requires the integrated development plan to form the basis for the annual report, therefore requiring consistency of objectives, indicators and targets between planning and reporting documents. A total of 20% of the reported indicators and targets were not consistent with those in the approved integrated development plan. This was due to lack of adequate review by management of reported performance information against predetermined objectives detailed in the SDBIP.
28. Section 25(2) of the MSA determines that an integrated development plan adopted by a municipal council may be amended in terms of section 34 and remains in force until an integrated development plan is adopted by the next elected council. Therefore, if the integrated development plan is changed in-year this process has to take place in accordance with the process as prescribed per section 34 of the MSA. A total of 50% of targets reported in the annual performance report were changed in-year without adoption by the council of the municipality. This was due to lack of review by management to ensure that all approved changes made via the mid-year deviation and alignment process were implemented and reported on accurately in the performance report.

#### **Performance targets not specific**

29. The FMPPi requires that performance targets be specific in clearly identifying the nature and required level of performance. A total of 27% of the targets were not specific in clearly identifying the nature and the required level of performance. This was due to a lack of regular training on FMPPi to enable application of the principles.

### **Reliability of reported performance information**

30. The FMPPi requires auditees to have appropriate systems to collect, collate, verify and store performance information to ensure valid, accurate and complete reporting of actual achievements against planned objectives, indicators and targets. Significantly important targets were not reliable when compared to the source information or evidence provided. This was due to a lack of standard operating procedures or documented system descriptions for the accurate recording of actual achievements, monitoring of the completeness of source documentation in support of actual achievements and frequent review of the validity of reported achievements against source documentation.

## **Development priority 3: Good governance cluster**

### **Usefulness of reported performance information**

31. I did not raise any material findings relating to the usefulness of the reported performance information for development priority 3: Good governance cluster.

### **Reliability of reported performance information**

32. I did not raise any material findings relating to the reliability of the reported performance information for development priority 3: Good governance cluster.

## **Additional matter**

33. I draw attention to the following matter:

## **Achievement of planned targets**

34. Refer to the annual performance report on pages x to x; x to x; x to x and x to x for information on the achievement of planned targets for the year. This information should be considered in the context of the material findings on the usefulness and reliability of the reported performance information in paragraphs 24 to 32 of this report.

## **Compliance with legislation**

35. I performed procedures to obtain evidence that the entity has complied with applicable laws and regulations regarding financial matters, financial management and other related matters. My findings on material non-compliance with specific matters in key applicable laws and regulations as set out in the general notice issued in terms of the PAA are as follows:

## **Budget**

36. Expenditure was incurred in excess of the limits of the amounts provided for in the votes of the approved budget, in contravention of section 15 of the MFMA. The total unforeseen and unavoidable expenditure incurred exceeded R15 million in contraventions of Municipal Budget and Reporting Regulation 72.

## **Annual financial statements**

37. The consolidated and separate financial statements submitted for auditing were not prepared in all material respects in accordance with the requirements of section 122(1) of the MFMA. Material misstatements of non-current assets, revenue and irregular expenditure identified by the auditors in the submitted financial statements were subsequently corrected and the supporting records were provided subsequently, resulting in the financial statements receiving an unqualified audit opinion.

## **Revenue management**

38. An adequate management, accounting and information system was not in place which recognised revenue when it was earned, as required by section 97(1) (h) of the MFMA.

## **Procurement and contract management**

39. Contracts and quotations were awarded to bidders who did not submit a declaration on whether they are employed by the state or connected to any person employed by the state, as required by National Treasury's Municipal Supply Chain Management regulation (SCM regulation 13(c)).

40. Awards were made to providers who are in the service of other state institutions or whose directors/ principal shareholders are in the service of other state institutions, in contravention of section 112(j) of the MFMA and SCM regulations 44. Similar awards were identified in the prior year and no effective steps were taken to prevent or combat the abuse of the SCM process in accordance with SCM regulation 38(1).

41. Goods and services with a transaction value of below R200 000 were procured without obtaining the required price quotations as required by SCM regulation 17(a) and (c).



42. Goods and services of a transaction value above R200 000 were procured without inviting competitive bids, as required by SCM regulation 19(a). Deviations were approved by the accounting officer even though it was not impractical to invite competitive bids, in contravention of SCM regulation 36(1).

### **Expenditure management**

43. Money owing by the municipality was not always paid within 30 days of receiving an invoice or statement, as required by section 65(2)(e) of the MFMA.

### **Consequences management**

44. Not all instances of irregular expenditure incurred by the municipality was investigated to determine if any person is liable for the expenditure, in accordance with the requirements of section 32(2) of the MFMA.

### **Internal control**

45. I considered internal control relevant to my audit of the consolidated and separate financial statements, annual performance report and compliance with legislation. The matters reported below are limited to the significant internal control deficiencies that resulted in the findings on the annual performance report and the findings on non-compliance with legislation included in this report.

### **Leadership**

46. The accounting officer did not adequately exercise oversight responsibility regarding financial and performance reporting. The municipality did not have sufficient monitoring controls to ensure that financial and performance reports submitted for audit are accurate and complete.

### **Financial and performance management**

47. There is lack of proper record management system that provides for the maintenance of information reported in the financial statements and performance reporting. Non-compliance with laws and regulations such as the MFMA, SCM regulations and MSA regulations could have been prevented had compliance been properly reviewed and monitored.

### **Other reports**

### **Investigations**

48. Seventy cases (70) of alleged irregularities including fraud were investigated. The majority of these cases were investigated internally by the forensic section of the municipality's internal audit division. Of these, twenty eight (28) were finalised, thirteen (13) were closed due to lack of evidence and the remainder are at different stages of execution. The nature of the cases covered a wide spectrum of activities, namely, bribery, theft, financial corruption, tender irregularities and various other issues.

*Auditor-General*

Johannesburg

12 December 2014



AUDITOR-GENERAL  
SOUTH AFRICA

*Auditing to build public confidence*